

FIXED ASSETS AND INVENTORY CONTROL

Audit Report No. FAINV0111

February 3, 2011



**MENTAL HEALTH MENTAL RETARDATION
AUTHORITY OF HARRIS COUNTY**

Internal Audit Department

AUDITOR'S REPORT

Fixed Assets and Inventory Control

Harris County, Texas

Internal Audit Department

February 3, 2011

Henry E. Webb, CFE

Internal Auditor





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Re: Fixed Assets/Inventory Control
Audit Report No. FAINV0111

BACKGROUND

The Mental Health and Mental Retardation Authority of Harris County (MHMRA) has formal policies and procedures designed to ensure control and oversight related to recording, valuing, reporting and safeguarding inventory and that fixed assets are adequately accounted for. These policies and procedures were created to provide a mechanism to monitor, by a centralized fixed asset management system (AssetWin), the accountability, care, and disposition of those assets.

The obligation of a unit director or department head is to ensure that the Agency property within their custody is subject to proper use, care, safe-keeping, and disposition. This is inherent by the assignment to that position at any level and includes ensuring the security of all property with that unit or department, whether idle or in use. Additionally, this includes monitoring subordinates to ensure that their activities contribute to the proper support and accountability of site assigned property.

The obligation of staff entrusted with Agency property is best described as an end-user that ensures its proper use, care, and safekeeping. Direct responsibility results from a documented assignment as the accountable person for that asset.

Personal responsibility or obligation for the asset is inherent by all Agency personnel to exercise reasonable and prudent actions regarding the proper use, care, and safeguarding of Agency property in their physical possession or care. This applies to all property issued, used, acquired, or converted to a person's exclusive use.

The following highlights the provisions found in Policy and Procedures **BUS-R/I: 1.1 – F/B: 3.4:**

- All property and equipment are assigned to a unit location
- If property or equipment is to be used off premises, written approval must be obtained
- Property and/or equipment signed out to an employee becomes the financial responsibility of that employee
- MHMRA property shall be inventoried according to guidelines developed and in compliance with the State Property Law

- The numbering of all MHMRA property is to be done with metal tags, decalcomania transfers, or cloth tabs
- The property will be assigned a unique sequenced number
- The Accounting Department will forward a copy of the Voucher and Invoice to the Fixed Assets Manager (source document)
 - ❑ Numbered Property Tag – Each item is to be assigned a number and an identification tag is affixed.
 - ❑ Non-Numbered Property Tag – A non-numbered identification tag is affixed to items of less than \$5,000 value.
 - ❑ Numbered Property Register – A numerical list of all property is maintained showing inventory number, unit number, location number, description of property, and value of item. The Fixed Assets Manager maintains the location register.
 - ❑ Numerical Listing of All Properties – This is to be furnished to each person responsible for property, at least once a year.
- On an on-going basis, the person responsible for property at the unit will be sent a list of all property that he/she is responsible for on the property records
- There will be a physical inventory on a test basis throughout the year. All units and departments will be inventoried at least once during the year
- The person responsible for numbered property will notify the Fixed Assets Manager and the Purchasing Officer in writing when any property becomes surplus
- The Purchasing Officer will transfer the surplus property to a locked, secured place
- The Purchasing Officer will also be responsible for all salvage property
- Receipts from Agency sales go into the General Fund

Currently, MHMRA utilizes the Fixed Assets System called AssetWin, and maintains all fixed assets and required inventoried items in this system. The State of Texas requires MHMRA to safeguard property as described in the Fiscal Year 2011 Performance Contract and various requirements that are unique to particular grant documents:

DEPARTMENT OF STATE HEALTH SERVICES

Article 16, Section 16.01 Equipment Purchases. *“Contractor shall implement a capitalization threshold for personal property at \$5,000. Contractor shall manage controlled assets, to include facsimile machines, telecopiers, stereo systems, cameras, video recorder/laserdisc players, televisions, video cassette recorders, camcorders, desktop and laptop computers, and non-portable printers.”*

Section 16.02 Property Inventory. *“Contractor shall maintain a nonexpendable personal property (i.e., equipment) inventory. Contractor shall administer a program of maintenance, repair, and protection of assets under this Contract so as to assure their full availability and usefulness.”*

DEPARTMENT OF AGING AND DISABILITY SERVICES

Policy Number 1A & B Definition and Disposition of Equipment and Controlled Assets for Cost Reimbursement Sub Recipient Contracts. *“Controlled Assets are additional items that must be accounted for according to the following acquisition cost parameters:*

Item	Acquisition Cost
Firearms	Any
Copiers	More than \$500
Medical and Laboratory Equipment	More than \$500
Emergency Management Equipment	More than \$500
Media Equipment (such as but not limited to video recorders, cameras, CD players, TVs, VCRs, camcorders, DVD players)	More than \$500
Desktop and Laptop Computers	More than \$500
Printer (not portable)	More than \$500
Communication Devices and Systems (such as but not limited to FAX machines, cellular/mobile telephones, hand-held radios, Blackberry devices, pagers, telecopiers)	More than \$500

MHMRA's approach to asset management is to apply a standard business operating system through AssetWin regarding property control, accountability, responsibility, and general asset management. Additionally, management has tried to provide consistent asset transaction reporting procedures for maintaining and updating site inventory records.

In nearly every case, personnel employed by MHMRA are users of either fixed assets or those assets which require tracking. The policy and procedures provides specific guidance and procedures towards the proper use and care of such assets, including the disposition of stolen, lost, damaged or destroyed property. It further defines the accountability, responsibility, and liability of Agency personnel regarding property use, including the reporting of transactions necessary for the effective record maintenance of AssetWin.

Capital Assets

Capital assets with useful lives of more than one year are stated at cost. Donated capital assets are valued at their estimated fair market value on the date received. The Agency capitalizes assets with an initial, individual cost of \$5,000 or more. Depreciation is computed using the straight-line method over the estimated useful life of the assets. No depreciation is calculated on land. Depreciation expense on assets specifically identified with a function/program is included in its direct expenses, and the depreciation on shared capital assets are included ratably.

The following asset lives are used:

Buildings	45 years
Building Improvements	20 years
Furniture, Machinery, Vehicles and Other Equipment	5-20 years
<u>Telecommunications and Peripheral Equipment</u>	<u>10 years</u>

Table 1 presents total Capital Assets Used in the Operation of Governmental Funds

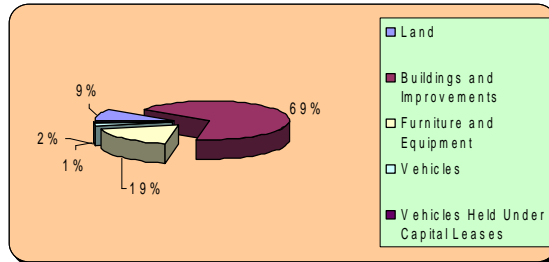
Table 1
MHMRA OF HARRIS COUNTY
Capital Assets Used in the Operation of Governmental Funds
Schedule of Changes by Function
For the Year Ended August 31, 2010

Function	Governmental Fund Capital Assets August 31, 2009	Additions	Retirements	Governmental Fund Capital Assets August 31, 2010
Mental Health	\$14,486,785	\$810,346	\$ <53,434>	\$ 15,243,697
Mental Retardation	7,574,842	249,175	<97,273>	7,726,744
Child and Adolescent	3,340,358	187,551	<10,722>	3,517,187
Crisis Center	3,481,588	48,112	<85,824>	3,443,876
Administration	6,633,576	1,396,777	<46,493>	7,983,860
Total Governmental Fund Capital Assets	<u>\$35,517,149</u>	<u>\$2,691,961</u>	<u>\$ <293,746></u>	<u>\$ 37,915,364</u>

Source: Agency CAFR for Fiscal Year Ended August 31, 2010.

Exhibit 1 presents total Capital Assets as a percentage (%) by group.

Exhibit 1
MHMRA of Harris County
Total Fixed Assets as a Percentage (%) by Group
As of September 30, 2010



OBJECTIVES

The overall objectives of the audit were to determine whether the departments:

- Managed and used resources in an efficient, effective, and economical manner
- Administered funds in compliance with applicable laws, regulations, policies and procedures
- Implemented internal controls to prevent or detect material errors and irregularities

The specific objective in this audit was to:

- Assist management with the assessment of the adequacy of internal controls related to recording, valuing, reporting, and safeguarding the Agency's inventory and fixed assets.

SCOPE

The scope of the work did not constitute an evaluation of the overall internal control structure of the units. The examination was designed to evaluate and test compliance with established policies and procedures and to test the internal control over tested areas and material. The audit scope was from March 1, 2010 through September 30, 2010.

Department management is responsible for establishing and maintaining a system of internal controls to adequately comply with approved policies and procedures. The objectives of an internal control system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or theft, and that transactions are executed in accordance with management's authorization and are recorded properly.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected in a timely manner. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with procedures may deteriorate.

The purpose of the audit report is to furnish management independent, objective analyses, recommendations, and information concerning the activities reviewed. The audit report is a tool to help management discern and implement specific improvements. The audit report is not an appraisal or rating of management.

Although due professional care in the performance was exercised, this should not be construed to mean that unreported noncompliance or irregularities do not exist. The deterrence of fraud is the responsibility of management. Audit procedures alone, even when carried out with professional care, do not guarantee that fraud will be detected. Specific areas for improvement are addressed later in this report.

Other minor findings, not included in this report, have been communicated to management and/or corrected during the audit process. Internal Audit would like to thank management and staff for their cooperation throughout the audit.

METHODOLOGY

In order to meet the objectives, Internal Audit flowcharted and evaluated controls over the acquisition, accounting, transfer and disposal of assets, and reviewed policies and procedures for compliance and completeness. MHMRA staff were interviewed and audit tests and procedures were conducted as considered necessary.

The sample size and selection were statistically generated using a desired confidence level of 95%, expected error rate of 5%, and a desired precision of +/-5%. Statistical sampling was used in order to infer the conclusions of test work performed on a sample to the population from which it was drawn and to obtain estimates of sampling error involved. When appropriate, judgmental sampling was used to improve the overall efficiency of the audit.

STATEMENT OF AUDITING STANDARDS

The audit was conducted in accordance with generally accepted government auditing standards (GAGAS). Those standards require that Internal Audit plan and perform the audit to afford a reasonable basis for the judgments and conclusions regarding the organization, program, activity, or function under audit. An audit also includes assessments of applicable internal controls and compliance with requirements of laws and regulations when necessary to satisfy the audit objectives. An audit also includes assessing the estimates, judgments, and decisions made by Agency management. It is believed that this audit provides a reasonable basis for the findings, conclusions, and recommendations.

RESULTS

As a result of the audit procedures and surveys conducted, it was determined that controls over inventory and fixed assets do not meet Agency policy and procedures, that the controls are not adequate and do not provide reasonable assurance that the Mental Health and Mental Retardation Authority of Harris County's fixed assets and inventory are accurately recorded, valued, reported, and adequately safeguarded. Areas that were noted that needed improvement over internal control are discussed below.

FINDING

Stock Room Responsibility, Reallocation of Resources, Review of Fixed Assets Software

The Fixed Assets Department, by definition is ultimately responsible for not only maintaining an accurate list of Agency owned assets (over 5,000) and required inventory items, but also keeping the policy and procedures that govern the control of those assets updated and relevant.

The Physical Inventory Reconciliation is the most important phase of the inventory. Inventory of these assets takes place at 33 Agency owned sites throughout Harris County. Inventory counts will produce assets expected but not found, found but not expected and assets located in different locations than the database has indicated or under the control of a different unit than that indicated in the database.

Approximately 20% of inventoried items tested were not found to be either in the proper location or assigned to the correct employee

Due to limited space and a basic unfettered access to assets held in the Agency Stock Room, confusion as to the whereabouts of Agency assets and inaccurate data in AssetWin has almost rendered the data of AssetWin unreliable.

RECOMMENDATION

- It is recommended that the control of the Agency Stock Room located at 7011 SW Freeway become the responsibility of the Fixed Assets Department. The Fixed Assets Department should immediately develop detailed policies and procedures to inventory and control all assets assigned to this area which also includes the entrance and exit of all assets.
- It is recommended that the Purchasing Department continue to receive items with the Fixed Assets Department. The Fixed Assets Department is charged with tagging, scanning and the ultimate confirmation or cross control by the Purchasing Department staff, until a decentralized receiving process can be developed by the Fixed Assets Department.
- It is recommended that the Fixed Assets Department review the assignment of all FAD's and reallocate inventory control workload to provide a more efficient and economical allocation of staff time. This reallocation includes a decentralization of responsibility of Fixed Assets to Agency Units (FADs) by use of an "Enterprise" Fixed Assets System. This process should provide for the responsibility of the FADs to include that of monitors for the assets under their control and with reporting of those results to the Fixed Assets Department.
- It is recommended that up to 2.0 additional FTE be added to the Fixed Assets Department to accomplish and address the lack of asset control throughout the Agency. Currently a 1.5 FTE allocation within the Fixed Assets Department is responsible for over 5,000 assets, 33 Agency locations, and approximately 11,000 transactional relocations each year, as well as the required reconciliations. It is impossible to maintain an adequate reviewed or controlled of Agency assets. These additional resources would be best allocated in the area of fixed assets operations and monitoring/analysis.
- It is recommended that all policy and procedures directly impacting fixed assets/inventory items within the Agency be reviewed and revised as the Fixed Assets Department revamps the decentralization of Agency receiving and monitoring of items. These policies and procedures should be clarified, solidified and provided to all FADs and other Agency staff that are required to purchase, receive, tag or have direct responsibility for these items.
- It is recommended that when a deliberate violation of established Fixed Assets Policy and Procedure is reported, that immediate disciplinary action take place, up to and including termination.

Management Response (Fixed Asset Department)

"We agree with the findings of this audit. Steps that have been taken to implement these recommendations include the planned construction of a Fixed Asset stock room on the first floor at 7011 Southwest Freeway where equipment will be received and tagged. Procedures for receiving fixed assets has been reviewed and revised (see attached flowchart).

Additionally, an analysis of the asset to FAD ratio is being conducted to provide more uniformity and efficiency in the utilization of staff time. Furthermore, one (1) inventory clerk is currently being recruited at this time to improve the control of fixed assets. An assessment of personnel needs will be conducted after the deployment of this resource.

We are currently reviewing, consolidating, and revising all the disparate policies bearing on fixed assets. It is our intent that when this is finalized, violation of these policies will result in disciplinary action."

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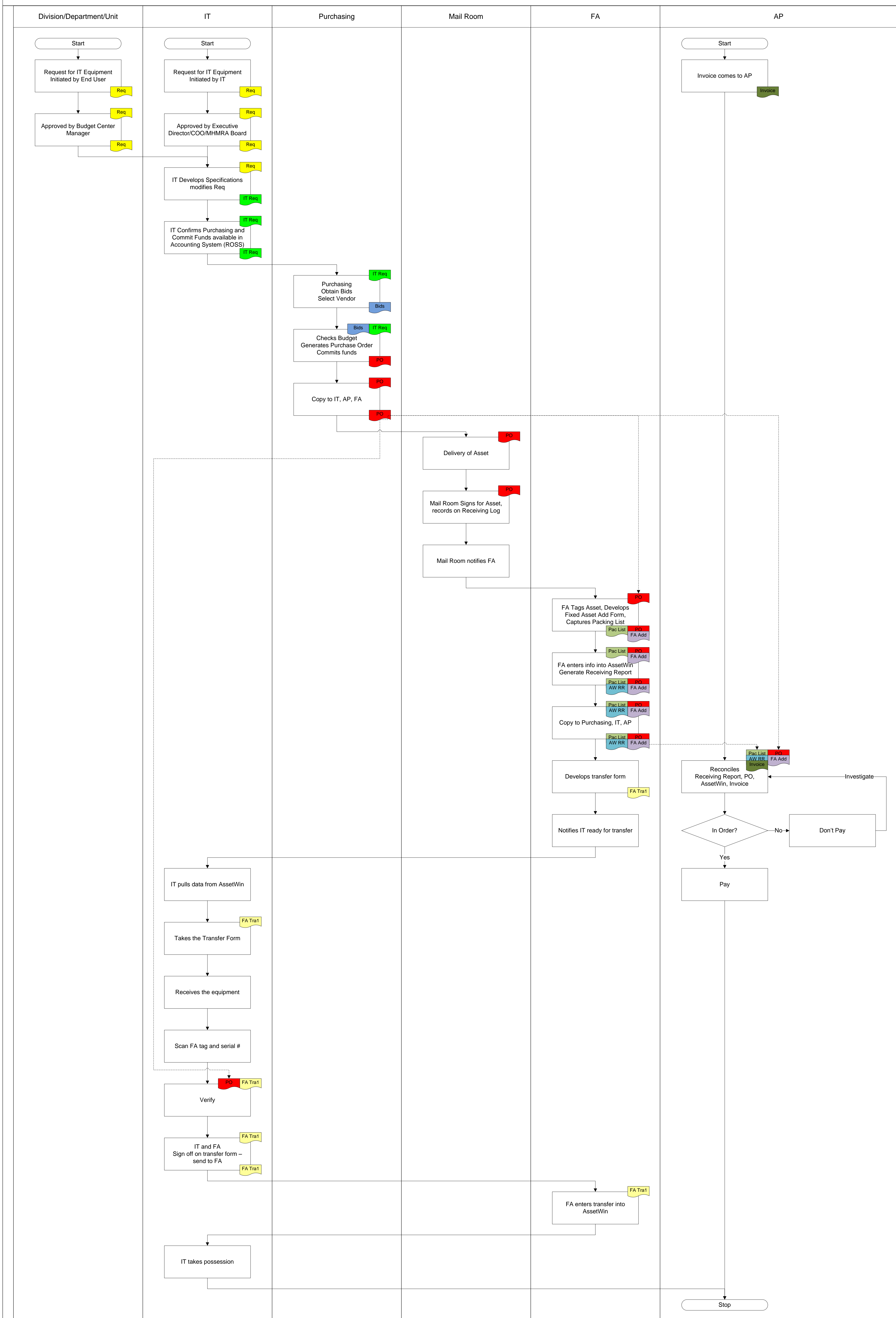
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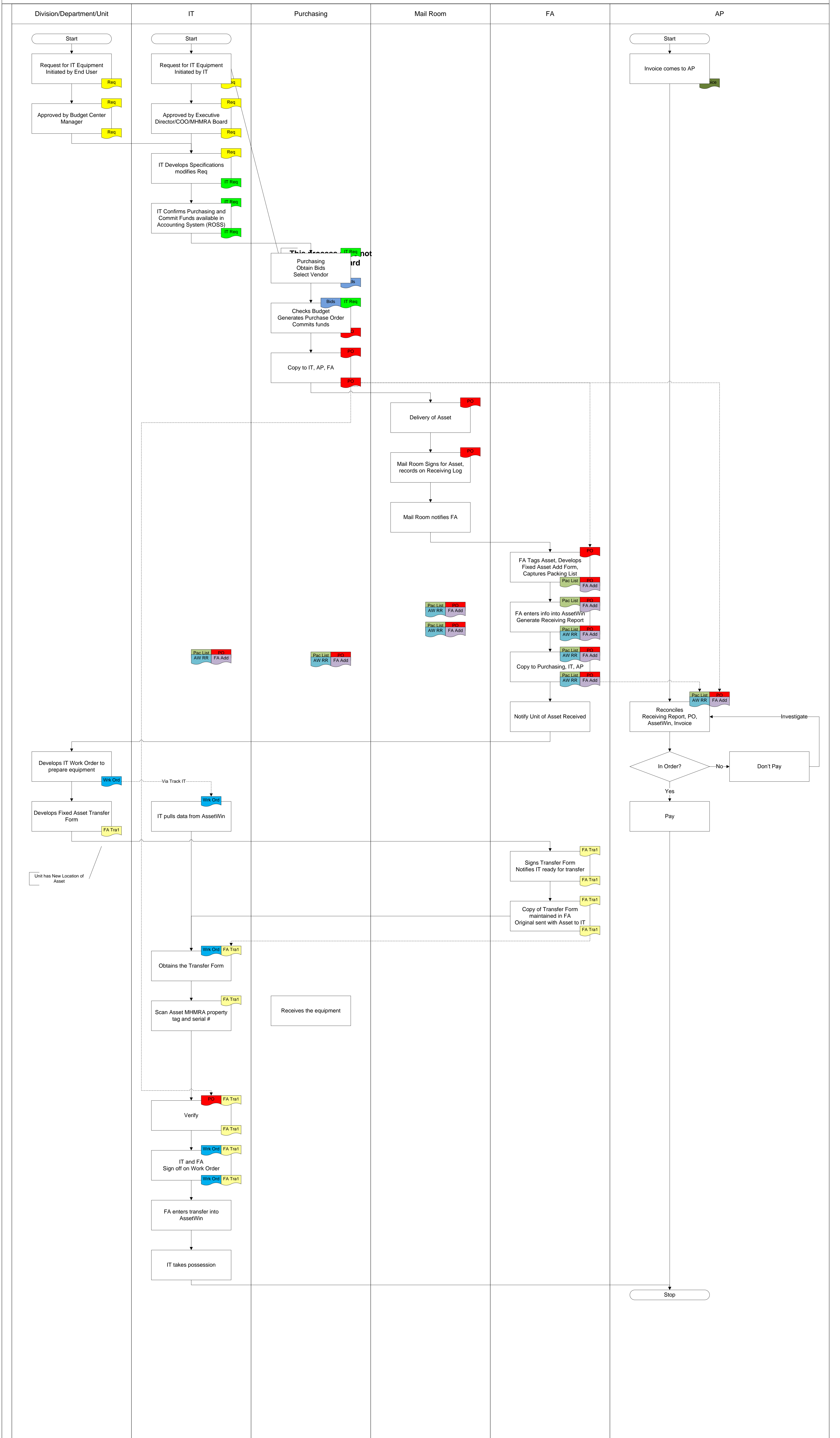
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IT Equipment Acquisition Process



IT Equipment Acquisition Process



ATTACHMENT A
SUMMARY OF RECOMMENDATIONS
February 3, 2020

Unit: Fixed Assets/Inventory Control		
Area: Audit		
Inherent Risk: Low Moderate High	Control Environment: Well Controlled Acceptable Poorly Controlled	Overall Risk: Low Moderate High
Type of Procedures: Audit		
Scope: <ul style="list-style-type: none"> * Using Internal Control Evaluation (ICEs) forms, documented internal controls * Conducted a preliminary survey reviewing applicable policies and procedures, etc. * Interviewed various staff, obtained understanding of management controls * Examined detailed receipts, vouchers, and supporting documentation 		
Priority Rating:	Audit Recommendations:	
1	FA Department control Storage Room located at 7011 SW Freeway	
1	Purchasing/FA control receiving, tagging and processing of items	
1	FA should review role of Fixed Assets Designee (FADs) for decentralized role	
1	FA should receive additional support of 2.0 FTE	
1	FA should review P&P and amend for a decentralized process	
1	Agency take decisive action when P&P are circumvented	
Follow-up: On-going (unannounced)		

Priority Rating

1. Implement immediately (30 - 90 days) - Serious internal control deficiencies or recommendations to reduce cost, maximize revenues, or improve internal controls that can be easily implemented.
2. Work towards implementing (6 - 18 months) - Less serious internal control deficiencies or recommendations that can not be implemented immediately because of constraints imposed on the unit (i.e., budgetary, technological constraints).
3. Implement in the future (2 - 3 years) - Recommendations that should be implemented but that can not be implemented until significant and/or uncontrolled events occur (i.e. legislative changes, buy and install major systems, requires third party cooperation).